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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 634

THEODORE A. MEYERS and wife, ALICE V. MEYERS,
Petitioners

v.

THE UNITED STATES, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

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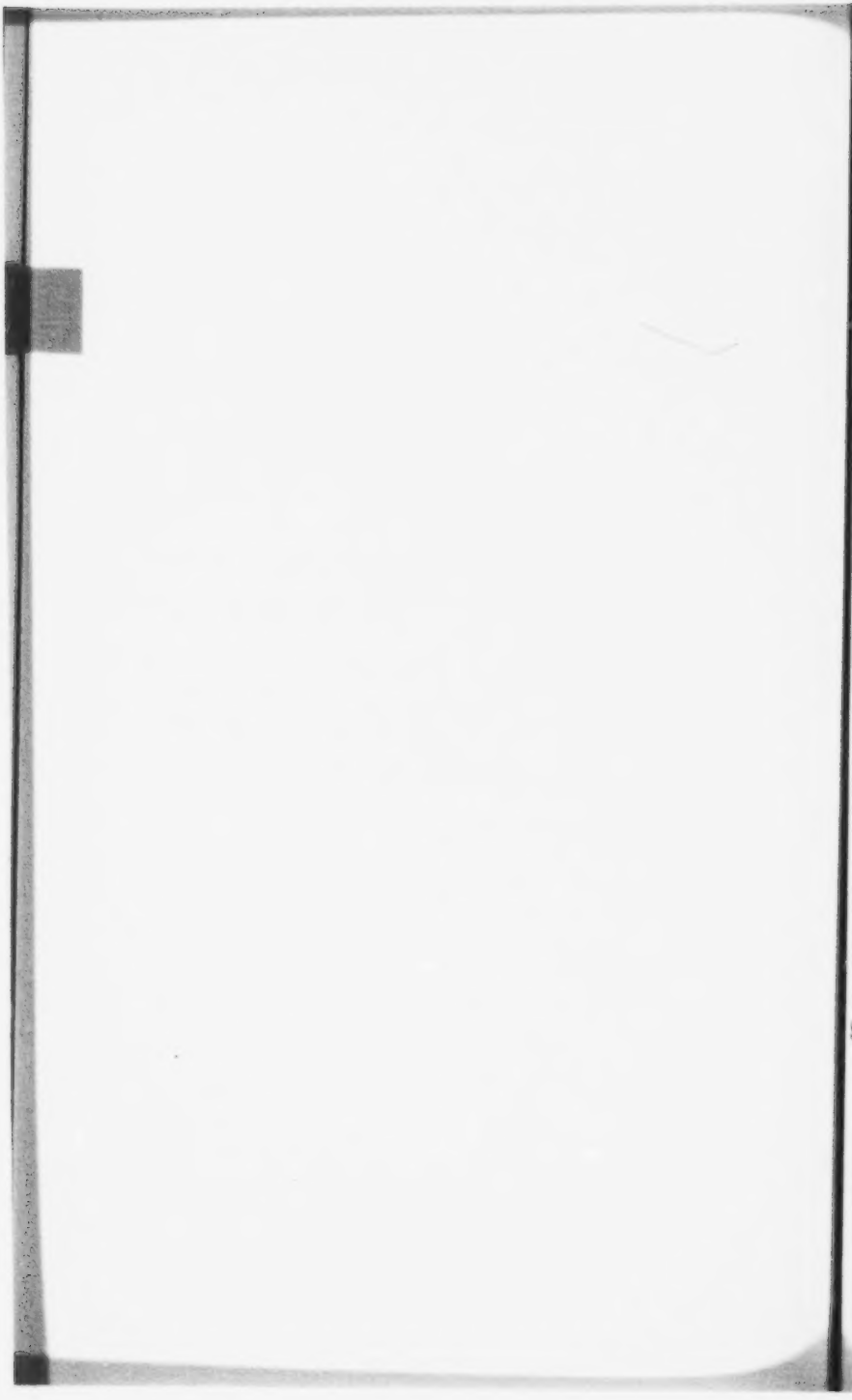

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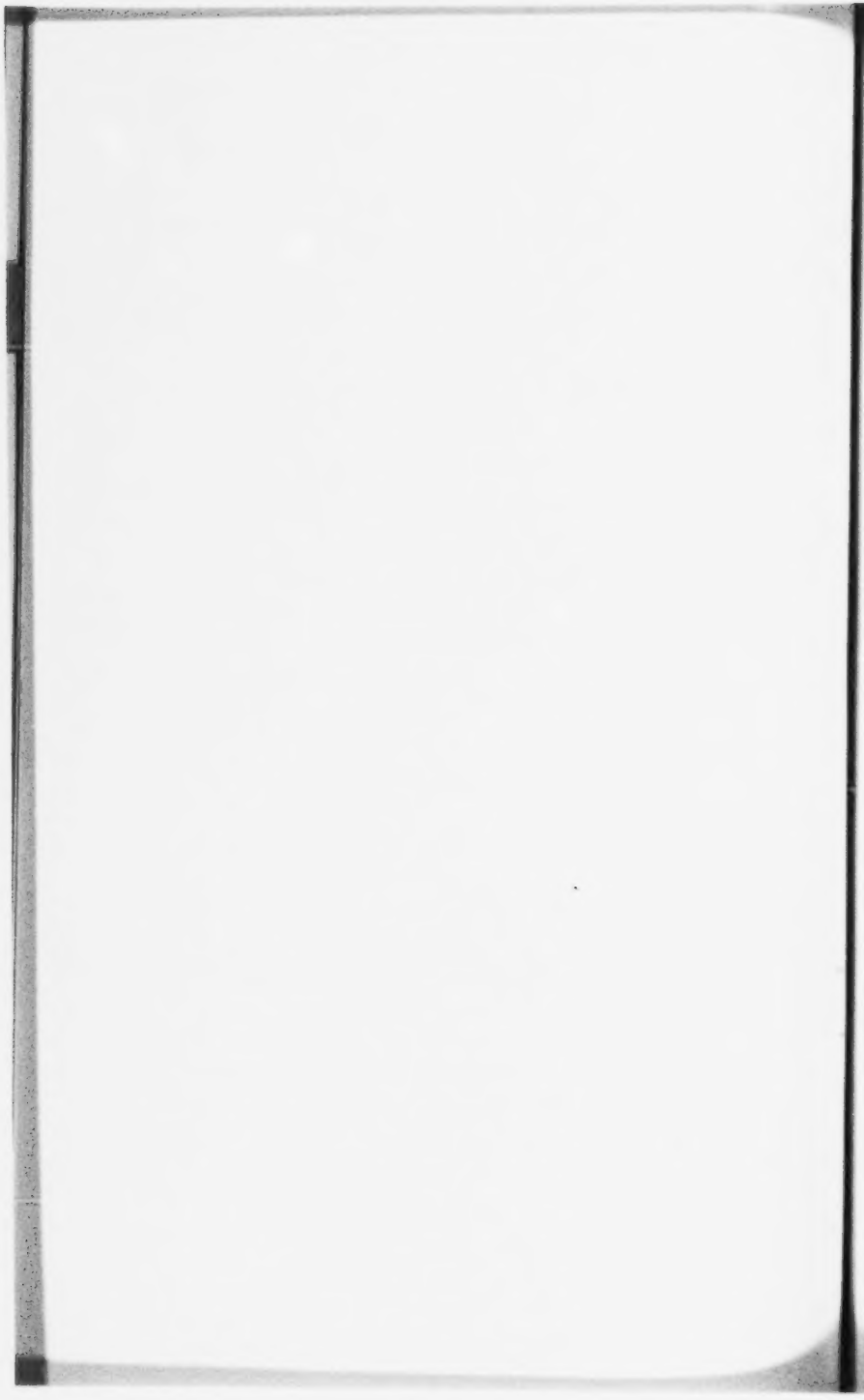

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Theodore A. Meyers and Alice V. Meyers, the petitioners, pray that a writ of certiorari issue to review the judgment of the United States Court of Claims in the above-entitled cause entered October 2, 1956.

OPINIONS BELOW

The opinions of the United States Court of Claims are printed at pages 1a through 20a of Appendix A to this petition. The reports of the Commissioner are printed at pages 20a through 31a of Appendix B to this petition.

Motion for re-hearing and order of the Court are printed at pages 32a and 33a of Appendix C to this petition.

Paragraph 8 of the stipulation of facts filed with the Court below are printed at pages 33a and 34a in Appendix D to this petition.

Exhibit A attached to the Statutory Notice of Deficiency is printed at pages 35a and 36a in Appendix E to this petition.

JURISDICTION

The judgment of the Court below was entered October 2, 1956 (App. A, page 33a infra). Jurisdiction of this Court is invoked under 28 U.S.C. 1254 (1).

QUESTIONS PRESENTED

I. Whether the Court below, by its decision, sanctioned the taking of property in an arbitrary manner by upholding a patently defective net worth computation employed by the Commissioner of Internal Revenue in determining petitioners' income tax liability for the calendar year 1948.

II. Whether the increasing of petitioners' net worth for the calendar year 1948 by adding thereto a nonbusiness bad debt in the amount of $43,159.99, sustained in such year upon investments made in prior years and for which no deduction was claimed by petitioners, constitutes such an arbitrary determination and collection of taxes that, if permitted to stand, the judgment of the Court below would do violence to the concept of fairness and equality upon which our system of jurisprudence is founded.

III. Whether the Court below, by refusing to permit petitioners "to explain the discrepancies in the case," referred to by the Court below in its opinion, constitutes a substantial denial of due process of law.

STATUTES

The applicable provisions of the Internal Revenue Code (1939) are herein set forth.

STATUTES INVOLVED

Internal Revenue Code of 1939:

SEC. 22. GROSS INCOME.

(a) [as amended by Sec. 1 of the Public Salary Tax Act of 1939, c. 59, 53 Stat. 574] *General Definition.*—"Gross income" includes *gains* profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of interest in such property; also from interest rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. ***

* * * * *

(26 U. S. C. 1952 ed., Sec. 22.)

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as

in the opinion of the Commissioner does clearly reflect the income. If the taxpayer's annual accounting period is other than a fiscal year as defined in section 48 or if the taxpayer has no annual accounting period or does not keep books, the net income shall be computed on the basis of the calendar year.

(26 U. S. C. 1952 ed., Sec. 41.)

SEC. 51. INDIVIDUAL RETURNS.

(a) [as amended by Sec. 11(a) of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231, and Sec. 202(c)(1) of the Revenue Act of 1948, c. 168, 62 Stat. 110] *Requirement.*—Every individual having for the taxable year a gross income of $600 or more shall make a return, which shall contain or be verified by a written declaration that it is made under the penalties of perjury. Such return shall set forth in such cases, and to such extent, and in such detail, as the Commissioner with the approval of the Secretary may by regulations prescribe, the items of gross income and the deductions and credits allowed under this chapter and such other information for the purpose of carrying out the provisions of this chapter as may be prescribed by such regulations.

(b) [as amended by Sec. 303 of the Revenue Act of 1948, *supra*] *Husband and Wife.*—

(1) *In general.*—A husband and wife may make a single return jointly. Such a return may be made even though one of the spouses has neither gross income nor deductions. If a joint return is made the tax shall be computed on the aggregate income and the liability with respect to the tax shall be joint and several.

* * * * *

(26 U. S. C. 1952 ed., Sec. 51)

SEC. 54. RECORDS AND SPECIAL RETURNS.

(a) *By Taxpayer.*—Every person liable to any tax imposed by this chapter or for the collection thereof, shall keep such records, render under oath such statements, make such returns, and comply with such rules and regulations, as the Commissioner, with the approval of the Secretary, may from time to time prescribe.

* * * * *

(26 U. S. C. 1952 ed., Sec. 54.)

SEC. 275. PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION.

* * * * *

(a) *General Rule.*—The amount of income taxes imposed by this chapter shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

* * * * *

(26 U. S. C. 1952 ed., Sec. 275.)

SEC. 293. ADDITIONS TO THE TAX IN CASE OF DEFICIENCY.

(a) *Negligence.*—If any part of any deficiency is due to negligence, or intentional disregard of rules and regulations but without intent to defraud, 5 per centum of the total amount of the deficiency (in addition to such deficiency) shall be assessed, collected, and paid in the same manner as if it were a deficiency, except that the provisions of section 272(i), relating to the prorating of a deficiency, and of section 292, relating to interest on deficiencies, shall not be applicable.

* * * * *

(26 U. S. C. 1952 ed., Sec. 293.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

> Sec. 29.54-1 [as amended by T. D. 5381, 1944 Cum. Bull. 188]. *Records and Income Tax Forms.* —Every person subject to the tax, except persons whose gross income (1) consists solely of salary, wages, or similar compensation for personal services rendered, or (2) arises solely from the business of growing and selling products of the soil, shall, for the purpose of enabling the Commissioner to determine the correct amount of income subject to the tax, keep such permanent books of account or records, including inventories, as are sufficient to establish the amount of the gross income and the deductions, credits, and other matters required to be shown in any return under chapter 1. Every organization exempt from tax under section 101 but required by section 54(f) to file an annual return shall keep such permanent books of account or records, including inventories, as are sufficient to show specifically the items of gross income, receipts, and disbursements, and such other information as is required by section 29.101-2. The books or records required by this section shall be kept at all times available for inspection by internal-revenue officers, and shall be retained so long as the contents thereof may become material in the administration of any internal-revenue law.
>
> * * * * *

STATEMENT

On February 8, 1952, and without any prior notice thereof, the Commissioner of Internal Revenue filed liens against petitioners' real and personal property by virtue of a jeopardy assessment totaling $29,439.33 allegedly constituting a deficiency in income taxes, penalty and interest for the calendar year 1948 in the respective amounts of $24,052.82, $1,202.64, and $4,-

183.87. The total assessment was paid by petitioners on February 20, 1952.

On March 6, 1952, a statutory notice of deficiency (90-day letter) reflecting computations of income tax liability for 1948 and over-assessments for the years 1949 and 1950 was mailed to the petitioners. Attached to this notice of deficiency was a computation of net worth identified as Exhibit A (Appendix E). This computation clearly shows that the principal cause for the deficiency was the addition of the sum of $43,159.99 representing a non-business bad debt sustained by the petitioners in 1948 upon investments made by them in years prior to 1948. The over-assessments determined for the calendar years 1949 and 1950 were likewise determined by means of the net worth method. The deficiency for the year 1948 was asserted to be $24,-052.82 whereas the over-payments for the years 1949 and 1950 were ascertained to be $1,665.66 and $269.16 respectively.

On March 14, 1952, petitioners filed a claim for refund in the amount of $34,276.43 for the calendar year 1948. For the purpose of the proceeding in the Court below, petitioners claimed that the sum of $29,439.33 was wrongfully assessed and collected from them for the calendar year 1948.

Condensing the data contained in the net worth computation, it is found that petitioners allegedly understated their income in the years 1948 by $49,-394.63. Of this amount, $43,159.99 represented a non-business bad debt which was added to the petitioners' net worth for that year (Stips. Para. 8—Appendix D). The use of the net worth also results in the over-reporting of income by the petitioners for the years 1949 and 1950 in the respective amounts of $1,000 and $11,583.12.

As actually constructed, the net worth method could not result in a deficiency for the year 1948 in the amount presently existing, without also conceding that petitioners over-reported their income for the years 1949 and 1950. It becomes self-evident, of course, that by adding the sum of $43,159.99 (non-business bad debt) to petitioners' net worth in 1948 it actually forces into existence the deficiency as we now know it. Inasmuch as petitioners had not claimed this loss in the year 1948 or prior thereto, there is no question, therefore, as to whether or not such a loss should or should not be allowed.

REASONS FOR GRANTING THE WRIT

1. In sustaining the method of assessing and collecting income taxes for the calendar year 1948, the Court below has actually sanctioned the arbitrary and capricious use of authority in contravention of well established concepts inherent in our form of government.

2. It is apparent that the net worth method employed by the Commissioner of Internal Revenue is incorrect. This is so not only because a non-business bad debt in the amount of $43,159.99 was added to petitioners' net worth in 1948, but also because petitioners' assets and liabilities remained relatively constant for the period in question. This fact is more graphically illustrated in the following summary:

	12/31/47	12/31/48	12/31/49	12/31/50
Total Assets	$217,731.74	$192,606.10	$211,469.12	$206,749.43
Total Liabilities	35,052.32	34,256.00	33,401.08	31,854.41

3. The most significant feature impugning the accuracy of the net worth and which unquestionably demonstrates that petitioners are entitled to recover is the fact that a non-business bad debt sustained by them in the year 1948 was added to their net worth by the Commissioner of Internal Revenue in arriving at a deficiency for that year (App. E). This bad debt (loss) resulted from investments made by petitioners in prior years and the fact that it became worthless in 1948 should not serve as a justification on the part of the Commissioner of Internal Revenue to add it to petitioners' net worth at the end of 1948.

4. Aside from the fact that the sum of $43,159.99 has been erroneously added to petitioners' net worth in computing a deficiency, the net worth itself is not immune from criticism in other respects. The net worth reflects decreases in petitioners' net worth for the two years following that for which a deficiency had been determined. Presumably, the starting point was inaccurately ascertained; otherwise, the resulting computations would not be in opposition to each other. That is, a net worth does not increase and decrease and yet have the assets and liabilities remain relatively constant during the period. That is, it does not do so unless a mistake of some kind has been made. The principle that the starting point of a taxpayer's net worth must be clearly and accurately established has been recognized in other decisions. *Brodella* v. *United States,* 184 Fed. 2d 823 C.C.A. 6 (1950) This same principle was announced by this Court in the case of *Holland* v. *United States,* 348 U.S. 121, when, among other things, it stated, ". . . that an essential condition of this type of case (net worth) is the establishment with reasonable certainty of an opening net worth."

As to whether or not the burden of proof can be shifted upon petitioners under the circumstances prevailing herein, the Supreme Court of the United States, in the case of *Helvering* v. *Taylor,* 293 U.S. 507, said:

> "We find nothing in the statutes, the rules of the Board or our decisions that gives any support to the idea that the Commissioner's determination shown to be without rational foundation and excessive will be enforced unless the taxpayer proves he owes nothing or, if liable at all, shows the correct amount . . ."

Allied to this principle is that expressed by the Court of Appeals for the First Circuit in the case of *Thomas, Constantine, et al.* v. *Commissioner,* C.C.A. 1 (decided April 12, 1956, Prentice-Hall, Para. 72,592). In reversing the Tax Court of the United States on the question of the amount of cash on hand at the beginning of the net worth computation, the Court of Appeals commented upon certain passages contained in the opinion of the Tax Court. Those passages and the comment of the Court of Appeals are herewith set forth:

PASSAGES

> "The deficiencies were determined upon the assumption that Thomas had no cash on hand on January 1, 1943. The burden is upon the petitioners to prove the amount of cash on hand."

> "The record is at least equally consistent with the conclusion that he had no cash. The petitioners have shown no basis for a finding that they had any cash on hand at any of the critical dates, and accordingly we must sustain the respondent as to that matter."

COMMENT

"We believe that these quoted passages do not correctly state the law. The presumption which favors the determinations of the Commissioner is not to be regarded as meaning that any arbitrary figure assigned to the cash on hand account without support in the record must nonetheless be treated as conclusive in the absence of an affirmative showing by the taxpayer of the correct amount . . ."

CONCLUSION

Not only is the decision of the Court below clearly erroneous, it also espouses the proposition that losses are equivalent to taxable income and are subject to taxation when inserted in a net worth method even though no tax advantage had inured to the benefit of the taxpayer sustaining the loss. The premises being considered, therefore, petitioners earnestly pray that this honorable Court review the judgment of the United States Court of Claims.

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